

FDIC State Profile

Spring 2006

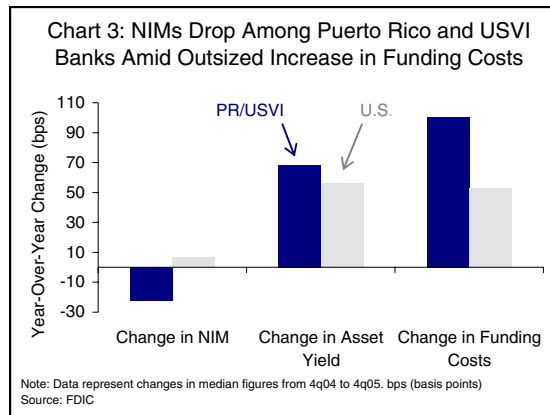
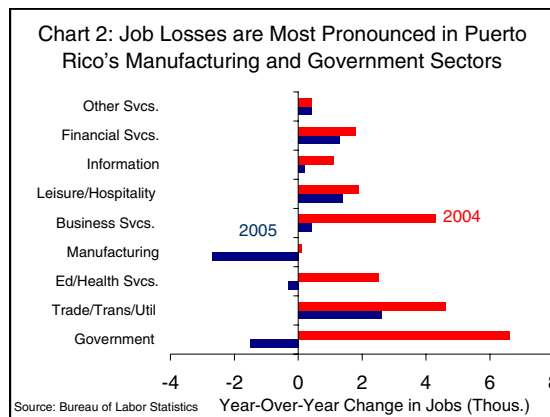
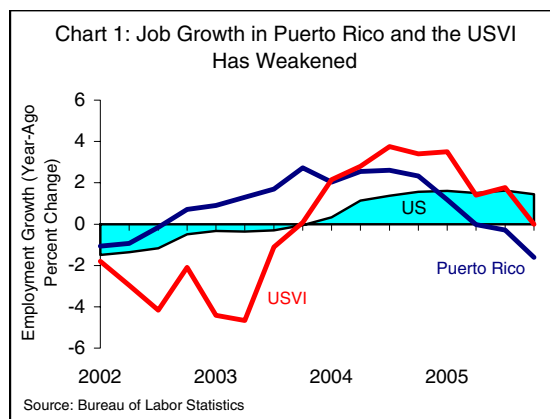
Puerto Rico and the U.S. Virgin Islands

Employment conditions in Puerto Rico and the U.S. Virgin Islands (USVI) have weakened.

- After achieving employment growth in excess of 2 percent in 2004, the highest annual rate since 1996, Puerto Rico lost 2,100 jobs (0.20 percent) in 2005, the first annual decline in three years. The rate of job loss accelerated during the year and reached negative 1.6 percent in the fourth quarter (see Chart 1).
- Job losses were broad-based as Puerto Rico's five largest industry sectors, by number of employed, experienced job contraction in the fourth quarter.
- Job growth in Puerto Rico's tourism related sectors was positive throughout 2005 but below growth rates achieved in recent years.
- Losses in manufacturing employment continued as Puerto Rico faced global competition (see Chart 2). Since 1995, Puerto Rico has experienced a greater rate of manufacturing job losses than the U.S., declining 27 percent compared with a 17 percent decrease for the nation. In the past few years, however, Puerto Rico has added jobs in capital intensive manufacturing areas such as pharmaceuticals and medical instrument manufacturing while losing jobs in labor-intensive manufacturing sectors.
- After adding 6,600 jobs in 2004, Puerto Rico's government sector shed 1,500 jobs during 2005, less than one percent of total government jobs. This marked the first time since 2001 that Puerto Rico's government sector trimmed payrolls. The government sector represents the largest employer on the Island, accounting for 29 percent of its total workforce.

Puerto Rico's pharmaceutical and tourism industries remain a source of strength.

- Puerto Rico's pharmaceutical industry continued to prosper despite the phase-out of federal tax incentives for U.S. firms. The pharmaceutical industry employs over 30,000 people in Puerto Rico and accounted for approximately 26 percent of the Island's gross product, compared with less than 2 percent in the United States.



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- Average wages for pharmaceutical workers were among the highest paid in Puerto Rico, and the industry accounted for 64 percent of all of the Island's exports in 2004.¹
- Puerto Rico's tourism also continued to improve. Total hotel registrations have been up for five consecutive years. Cruise ship visitors, although down slightly in the January to June period of 2005 compared with the prior year, were significantly higher than 2002 and 2003 period.

Puerto Rico and USVI banks reported lower profitability in 2005.

- Profitability reported by Puerto Rico and USVI institutions, as measured by return on assets, declined in 2005 compared with one year ago. Provisions for loan losses were below year-ago levels, but turned upward in the second half of 2005 consistent with credit quality trends. Net interest margins (NIMs) tightened in response to the flattened yield curve.
- A flatter yield curve in 2005 contributed to a decline in Puerto Rico and USVI's NIM to a degree more pronounced than for U.S. mainland institutions. Asset yields rose with higher short-term interest rates but were outpaced by the increase in funding costs (see Chart 3).
- The median cost of funds among Puerto Rico and USVI insured institutions increased at twice the rate of increase reported by U.S. mainland banks, driven by a higher mix of non-core funding. Typically, non-core funding is more sensitive to changes in interest rates than core deposits, and it has become more costly as short-term interest rates have risen.
- While funding costs are typically higher than in the United States, the spread between funding costs among Puerto Rico/USVI and U.S. institutions widened in 2005, reaching approximately 94 basis points in fourth quarter (see Chart 4).
- This spread may expand further in 2006 if short-term interest rates continue to rise. The last time short-term rates were near these levels, Puerto Rico/USVI funding costs exceeded U.S. costs by almost 140 basis points.

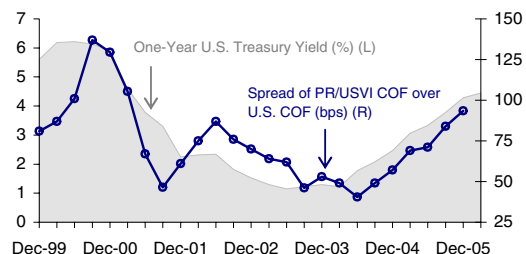
Credit quality in Puerto Rico and USVI has improved in recent years, but it exhibited moderate weakness in the second half of 2005.

- During the past three years, median credit quality ratios for institutions headquartered in Puerto Rico and USVI have generally improved (see Chart 5). However, early-stage loan delinquencies (30 to 89 days past due)

increased for the second consecutive quarter in fourth quarter 2005. Additionally, while the median loan charge-off rate was stable, some institutions reported higher charge-offs in the second half of 2005.

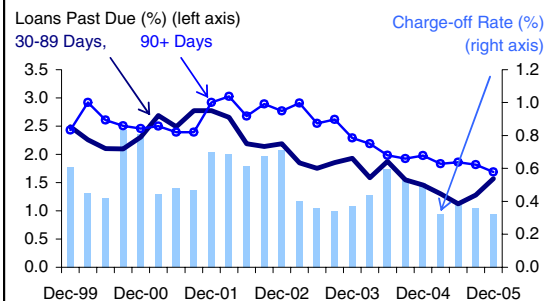
- Consistent with historical trends, median loan delinquency and charge-off rates for these institutions remained above the U.S. average. Recent employment weakness in the area could hinder further improvement in credit quality.

Chart 4: Puerto Rico and USVI Funding Costs are Exceeding U.S. Costs at an Increasing Pace



Notes: Cost of Funds (COF). U.S. Treasury rate data are quarterly averages through 4q05 and the monthly average for February 2006. Cost of funds data is through 4q05.
Sources: FDIC and Federal Reserve (Haver Analytics).

Chart 5: Loan Quality in Puerto Rico and USVI Has Improved in Recent Years



Source: FDIC

¹Source: Pharmaceutical Industry Association of Puerto Rico.

Puerto Rico and the U.S. Virgin Islands at a Glance

ECONOMIC INDICATORS (Change from year ago, unless noted)

Employment Growth Rates	Q4-05	Q3-05	Q4-04	2004	2003
Total Nonfarm (share of trailing four quarter employment in parentheses)	-1.6%	-0.3%	2.3%	2.4%	1.7%
Manufacturing (11%)	-5.2%	-2.4%	-1.1%	0.1%	-2.4%
Other (non-manufacturing) Goods-Producing (6%)	-8.6%	-6.1%	-0.3%	1.2%	-2.3%
Private Service-Producing (53%)	0.1%	0.8%	3.1%	3.1%	3.1%
Government (29%)	-1.7%	0.0%	3.0%	2.2%	1.8%
Unemployment Rate (% of labor force)	12.4	11.1	10.5	10.6	12.0

BANKING TRENDS

General Information	Q4-05	Q3-05	Q4-04	2004	2003
Institutions (#)	12	12	12	12	13
Total Assets (in millions)	103,183	101,651	93,703	93,703	78,275
New Institutions (# < 3 years)	0	0	0	0	0
Subchapter S Institutions	1	1	1	1	1

Asset Quality	Q4-05	Q3-05	Q4-04	2004	2003
Past-Due and Nonaccrual Loans / Total Loans (median %)	3.66	3.59	4.35	4.35	4.80
ALLL/Total Loans (median %)	1.13	1.12	1.28	1.28	1.55
ALLL/Noncurrent Loans (median multiple)	0.65	0.55	0.55	0.55	0.62
Net Loan Losses / Total Loans (median %)	0.47	0.27	0.44	0.51	0.37

Capital / Earnings	Q4-05	Q3-05	Q4-04	2004	2003
Tier 1 Leverage (median %)	6.93	6.72	6.88	6.88	6.78
Return on Assets (median %)	0.66	0.92	1.29	1.35	1.16
Pretax Return on Assets (median %)	0.91	1.15	1.44	1.65	1.37
Net Interest Margin (median %)	2.94	2.84	3.16	3.21	2.96
Yield on Earning Assets (median %)	5.94	5.72	5.26	4.98	5.35
Cost of Funding Earning Assets (median %)	3.18	2.90	2.17	2.00	2.36
Provisions to Avg. Assets (median %)	0.26	0.21	0.20	0.31	0.42
Noninterest Income to Avg. Assets (median %)	0.30	0.41	0.66	0.62	0.64
Overhead to Avg. Assets (median %)	1.77	1.66	2.20	2.13	2.23

Liquidity / Sensitivity	Q4-05	Q3-05	Q4-04	2004	2003
Loans to Assets (median %)	55.5	55.2	54.4	54.4	55.0
Noncore Funding to Assets (median %)	68.5	65.5	59.1	59.1	59.7
Long-term Assets to Assets (median %, call filers)	43.1	42.2	40.1	40.1	39.9
Brokered Deposits (number of institutions)	9	9	9	9	10
Brokered Deposits to Assets (median % for those above)	17.0	14.8	11.3	11.3	13.7

Loan Concentrations (median % of Tier 1 Capital)	Q4-05	Q3-05	Q4-04	2004	2003
Commercial and Industrial	99.0	123.2	83.9	83.9	143.3
Commercial Real Estate	209.0	201.8	175.6	175.6	194.0
Construction & Development	59.4	57.8	39.8	39.8	58.5
Multifamily Residential Real Estate	0.0	0.0	0.2	0.2	0.0
Nonresidential Real Estate	149.6	119.0	120.8	120.8	143.7
Residential Real Estate	217.6	242.5	251.7	251.7	306.0
Consumer	37.0	38.1	49.1	49.1	90.0
Agriculture	3.3	3.1	3.1	3.1	0.1

BANKING PROFILE

Largest Deposit Markets	Institutions in Market	Deposits (\$ millions)	Asset Distribution	Institutions
San Juan-Caguas-Guaynabo, PR	11	47,416	< \$250 million	2 (16.7%)
Ponce, PR	11	1,849	\$250 million to \$1 billion	0 (0%)
Mayaguez, PR	11	1,239	\$1 billion to \$10 billion	6 (50%)
Aguadilla-Isabela-San Sebastian, PR	8	1,181	> \$10 billion	4 (33.3%)
San German-Cabo Rojo, PR	4	702		